



INTEGRATED HEALTHCARE  
STRATEGIES™

# The After-Tax Protocol

*The After-Tax Solution to Pre-Tax Challenges*

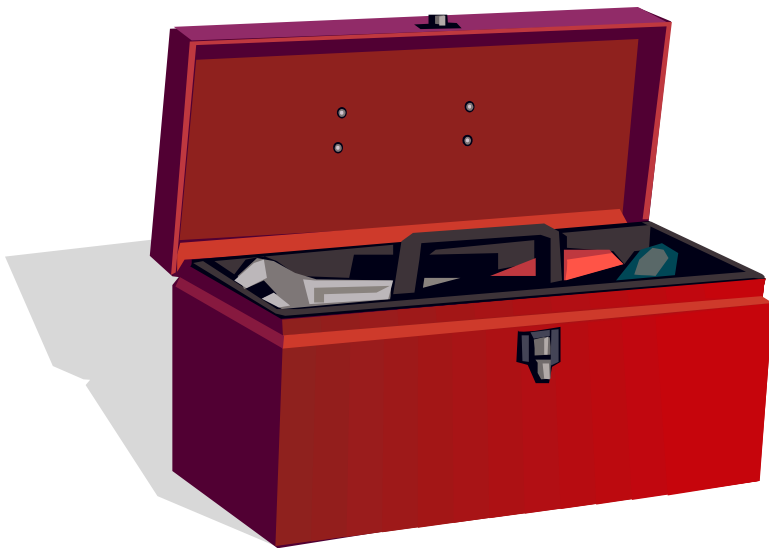
[www.IHStrategies.com](http://www.IHStrategies.com)

*Exclusive to Healthcare. Dedicated to People. SM*

## Deferred Compensation Has Been The Tool Of Choice in Addressing Numerous Business Challenges

Please dial: (616) 883-8055

Access code 177-318-085  
*to join the conference call if you haven't done so already.*



- ❑ Executive and Physician benefit planning (Sections 457(b), 457(f), 83)
- ❑ Retirement accumulation plans
- ❑ SERP funding
- ❑ Retention plans
- ❑ Physician and Executive recruitment incentives



# Pre-Tax Plan Design

Please dial: (616) 883-8055  
Access code 177-318-085  
*to join the conference call if you haven't done so already.*

**Employer**

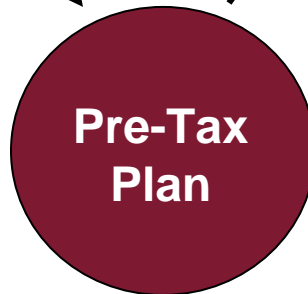


60% Pre-Tax Compensation

**Employee**



Retirement Distribution



**Pre-Tax Plan**

40% Deferred Taxation

**IRS**

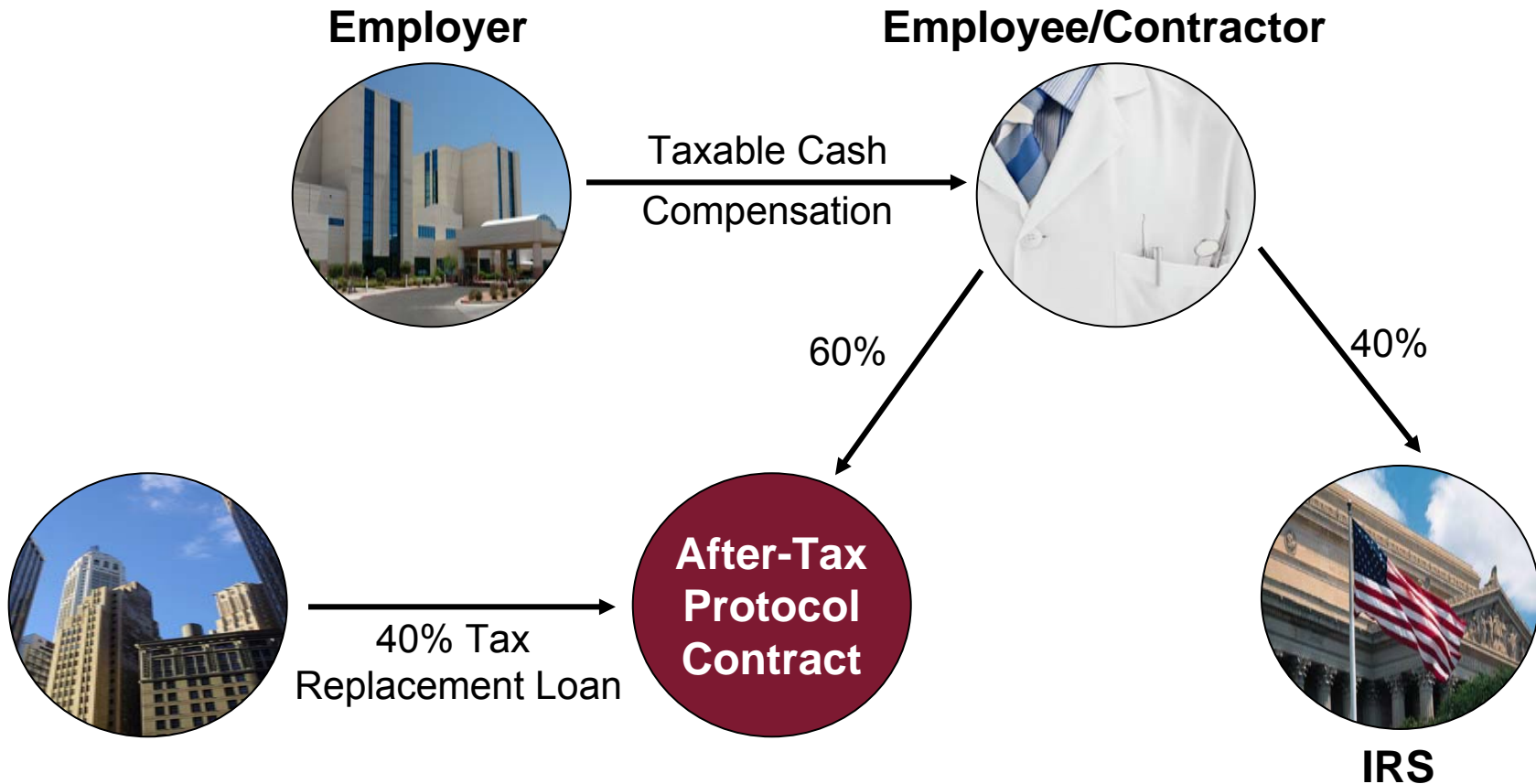


Plan funded by Employer dollars and IRS agreement to defer taxation



# After-Tax Protocol Design

Please dial: (616) 883-8055  
Access code 177-318-085  
*to join the conference call if you haven't done so already.*



Plan funded by Employee after tax dollars and Loan to replenish tax costs

## Today's Webinar

Please dial: (616) 883-8055

Access code 177-318-085  
*to join the conference call if you  
haven't done so already.*

### Unique After Tax Protocol Applications

- Physician Call Pay Solutions
- Physician Practice Acquisition Proceeds
- Retention Planning

### Our Panel Members are:

- Drew Erra, Senior Vice President
- Tom Becker, Senior Vice President
- Moderator: David Saltzman, Senior Director of Communications  
Integrated Healthcare Strategies





# Call Pay Security Solution

**After-Tax Protocol Application  
Number One**



## High Income Specialists Are Less Willing to Take Call as Part of Medical Staff Obligation

- ❑ Adverse payer mix in hospital
  - Growing uninsured population
  - No longer makes financial sense to provide care
- ❑ Physician-owned ancillary and technical services provide reasonable alternative to hospital
- ❑ Growing number of physicians willing to forfeit hospital privileges unless they receive additional value
- ❑ Hospitals being pressured to pay for call coverage to maintain medical staff and meet regulatory compliance



## The Potential Economic Impact of This Problem is Enormous

<b>Total Physicians in USA as of 2005 <sup>1</sup></b>	<b>817,440</b>
<b>Estimated Percent of Physicians On Call</b>	<b>50%</b>
<b>Estimated Physicians On Call</b>	<b>408,720</b>
<b>Estimated Average Annual On Call Payment</b>	<b>\$ 24,000</b>
<b>Potential Annual On Call Pay Obligation</b>	<b>\$ 9,809,280,000</b>

***<sup>1</sup>U.S. Department of Health and Human Services; “Physician Supply and Demand: Projections to 2020,” October 2006***



## Why Use the Call Pay Security Solution?

### Obtaining Physician On-call services

- Generally, a 1-year contract
- Cash payment for services

**Physicians leverage hospitals for increased payments with the threat of withholding on call service**



# Why Use the Call Pay Security Solution?

## The Alternative – Call Pay Security Solution

- ❑ Establishes fixed rate, long-term coverage agreement by specialty
- ❑ After-tax design allows use for both W-2 and 1099 physicians
- ❑ Organization can participate in the plan through interest repayment at a predetermined percentage in 5-year intervals to enhance value and build retention
- ❑ Interest repayment can be tied directly to on call performance
- ❑ Plan provides significantly more “value” to highly compensated specialists than straight cash payment



## Case Study

### The Problem:

- ❑ Call being provided by both W-2 and 1099 physicians
- ❑ FY07 call coverage pay \$16.5 Million
- ❑ FY08 expected to approach \$19 Million
- ❑ IHStrategies contacted to develop an alternative solution to meet their stated goals:
  - Reduce call pay amount by a minimum of \$3 million immediately
  - Control escalation in call pay amount
  - Provide long-term wealth accumulation for high income physicians
  - Develop incentive for physicians to actually meet contracted call obligation



## Case Study

### The Call Pay Security Solution:

- ❑ Reduce current call pay amount by 20%
- ❑ Use reduced rate to establish fixed 10-year payment stream
- ❑ Annual loans for 10 years to replace tax cost for participant
- ❑ System agrees to pay 25% of accrued interest at the end of each 5-year cycle assuming physician meets minimum call requirement
- ❑ System communicates change in amount and structure of all call pay agreements
- ❑ IHStrategies develops all illustrations and communication material
- ❑ IHStrategies meets with and enrolls participants
- ❑ Physician has complete control of distributions which are all income tax free



## Case Study: Apply the After-Tax Call Pay Solution

### The Results:

- ❑ Reduces immediate cost to hospital by \$3.3 million
- ❑ Converts cash call pay to fixed long-term plan
- ❑ Removes variability and eases budgeting
- ❑ Provides incentive for retention and meeting call obligation
- ❑ Delivers significantly more long-term value than after-tax investment by physician
- ❑ Plan would be most attractive to the most difficult physicians to secure (Orthopods, Neurosurgeons, Cardiologists, ENT, etc.)



## Cost Impact/Savings of After-Tax Protocol (ATP)

### INDIVIDUAL PHYSICIAN (AGE 50) 15 YEAR CALL PAY COST

	Year 1 Total	Year 5 Total	Year 10 Total	Year 15 Total
Current Call Pay Cost	\$24,000	\$120,000	\$240,000	\$360,000
Call Pay Cost using ATP	\$19,200	\$105,008	\$211,661	\$312,575
Client Savings with ATP	\$4,800	\$14,992	\$28,339	\$47,425

### TOTAL CALL PAY SAVINGS USING ATP (ALL PHYSICIANS)

Total Call Pay Savings	\$3,300,000	\$10,300,000	\$19,500,000	\$32,600,000
------------------------	-------------	--------------	--------------	--------------



## Cost Impact/Savings of After-Tax Protocol (ATP)

### AGE 65 PHYSICIAN RETIREMENT INCOME

<b>Current Call Pay</b>	<b>\$33,514 / Year for 15 Years<sup>1</sup></b>
<b>Call Pay using ATP</b>	<b>\$33,702 / Year for 15 Years<sup>2</sup></b>

- <sup>1</sup> Assumes physician invests after-tax income in no-load mutual funds earning 9% gross. Accumulation reduced by capital gains tax.
- <sup>2</sup> Assumes physician's after-tax income deposited in ATP, plus loan to reforest tax liability supplements the deposits. Tax loan repaid before income is taken. Nine percent (9%) gross rate of return.





# Acquisition Security Solution

## After-Tax Protocol Application Number Two



# Physician Recruitment – Environment & Challenges

## Recent Merritt–Hawkins Primary Care Physician Survey

- ❑ In 2007, 12.9% more Primary Care Physicians responded that
  - Over the next 5 years the job market will be more robust
- ❑ 79.2% of family practice physicians believe that
  - Due to poor reimbursement and other factors there will be a severe shortage of primary care physicians in 5 to10 years

**But what is the reality?**



# Physician Recruitment – Environment & Challenges

## Physician Supply & Demand: Projections to 2020

- A study commissioned by the Health Resources and Services Administration, U.S. Department of Health and Human Services in October 2006
  - General consensus
    - Overall physician supply per capita will remain stable over the next 15 years
    - Less agreement on future demand for physician services
  - Growing consensus that over the next 15 years the growth in requirements for physicians will outpace the growth in physician supply
  - Study evaluated both the projections of
    - Physician supply
    - Physician requirements



# Physician Recruitment – Environment & Challenges

## Physician Supply & Demand: Projections to 2020

- About 24,000 physicians complete their training annually
- Physicians leave the workforce through retirement, mortality, disability, and career change
- Current trends – physician population growth – 2005-2020
  - FTE primary care physician growth of 18%, 2005 – 2020
  - FTE non-primary care physician growth of 10%, 2005 - 2020
- FTE supply in some surgical specialties is expected to decline
  - General Surgery
  - Urology
  - Ophthalmology
  - Cardiology
  - And others



# A New Practice Acquisition Boom

## Health Systems Moving Into a Period of Aggressive Physician Employment

- ❑ Stark II Phase III regulations removed many exceptions currently allowing physicians ownership and self referral
- ❑ OIG removed many of the tools currently used by hospitals and physicians to joint venture
  - Under Arrangement Leasing
  - Per Click Joint Ventures
  - Mark Up Joint Ventures
- ❑ New generation of doctors not interested in assuming risks of private practice – want employment
- ❑ Private practice model becoming unsustainable for many specialties



# A New Practice Acquisition Boom

## This Employment Boom Differs from the 90s

- ❑ Focus on high income specialists, not just primary care
- ❑ Will require the acquisition of many specialty practices
  - High levels of ancillary incomes (MRI, CT, Mammography, etc.)
  - Large scale technical revenue (specialty hospitals, ambulatory surgery centers, endoscopy labs, etc.)
  - Significant professional revenues and incomes
- ❑ These acquisitions will require significant capital investment by acquiring organizations (typically in excess of \$500,000 per physician owner)



# A New Practice Acquisition Boom

## Boards of Directors Concerned about securing the transaction:

- ❑ Non-Competes
  - Adversarial start to relationship
  - Difficult to enforce if included
- ❑ Structured payment of proceeds
  - Limited under Stark II Phase III
  - Amount must be set in advance, not variable or tied to future performance
  - Difficult to sell to physician owners
- ❑ Deferral of acquisition proceeds
  - Traditional programs subject to IRS regulation including 409A
  - Traditional plans subject to insolvency risk of organization



# The Physician Acquisition Security Solution

## Overview

- ❑ Goal to shelter some or all of the proceeds for the seller while securing the transaction for the buyer
- ❑ Designate some or all of the proceeds be paid through the after-tax deferred compensation program
- ❑ After paying taxes, net amount placed into plan designed to fund the annual premiums over a 5-year period
- ❑ Annual tax replacement loans for the same time period returns value of proceeds to 100%
- ❑ Organization commits to paying some or all of the interest accrued on the premium loan based on continued service or performance targets



## Case Study

### Sample Transaction Details

- ❑ 17 multi-specialty physicians selling practice including all ancillary services and small specialty hospital
- ❑ Total purchase price of \$20 million determined by independent third party
- ❑ After transaction costs and debt retirement, each physician receives gross proceeds of \$900,000 in addition to ongoing compensation from employment agreement
- ❑ Purchaser seeking to secure transaction



# Case Study

## Sample Plan Design

- 50% of proceeds designated to Acquisition Security Solution
  - Gross proceeds of \$450,000 taxed and deposited into Acquisition Security Solution over 5 years
    - Net of \$270,000 @ 40% tax rate
  - Provides \$54,000 per year for 5 years
  - Lender provides \$36,000 per year for 5 years to restore taxes
- Organization agrees to pay % of interest cost every 5 years based on RVU production schedule
  - <75% projected RVUw – 0% of interest paid
  - 75% - 85% projected RVUw - 50% of interest paid
  - 85% - 95% projected RVUw – 75% of interest paid
  - 95% + projected RVUw – 100% of interest paid



## Case Study

### Benefits To The Buyer:

- Payment of the proceeds over 5 years limits physicians' access to capital to develop competing services
- Participation in interest payment develops golden handcuff retention value – less adversarial than non-competes
- Could support payment of higher value

### Benefits to Seller:

- Portable with no non-compete provision
- Provides significant tax advantage / significant wealth accumulation
- Not subject to acquiring organization's financial health
- Provides life insurance benefit to protect deferred assets





# Recruitment Security Solution

## After-Tax Protocol Application Number Three



# The Physician Recruitment Security Solution

## Overview

- ❑ Goal of developing immediate retention
- ❑ Create multi-year signing bonus plan using After-Tax Protocol
  - Annual taxable contribution for 5 - 10 years
  - Include annual contribution in reasonableness calculation
- ❑ Organization may participate in reducing premium loan cost at minimum 5-year intervals to further enhance retention value
- ❑ Organization may consider career service bonus to repay some or all of the principal



## Case Study

### Sample Transaction Details – Neurosurgeon Recruitment

- Age - 45
- Minimum Guaranteed income - \$650,000
- Compensation per Work RVU - \$ 70
- Production Threshold - 9028
  
- Annual Signing Bonus for 5 Years - \$ 65,000



# Sample Illustration

Funding Period Age 45 to Age 49						
Pre-Retirement Funding				Post-Retirement Income		
Age	Personal Deferral	Tax	Total Premium	Age	Annual Tax-Free Loan	Pre-Tax
		Replacement Loan				Equivalent Value
45	39,000	26,000	65,000	65	65,783	109,638
46	39,000	26,000	65,000	66	65,783	109,638
47	39,000	26,000	65,000	67	65,783	109,638
48	39,000	26,000	65,000	68	65,783	109,638
49	39,000	26,000	65,000	69	65,783	109,638
				70	65,783	109,638
				71	65,783	109,638
				72	65,783	109,638
				73	65,783	109,638
				74	65,783	109,638
				75	65,783	109,638
				76	65,783	109,638
				77	65,783	109,638
				78	65,783	109,638
				79	65,783	109,638
<b>Total</b>	<b>195,000</b>	<b>130,000</b>	<b>325,000</b>	<b>Total</b>	<b>986,745</b>	<b>1,644,575</b>
<b>Cash Value Net of Loan</b>				<b>Death Benefit net of Loan</b>		
	Cash Value at Age 65		\$1,031,389	Death Benefit at age 45		\$1,239,601
	Tax replacement loan + Interest		-\$407,614	Death Benefit at age 65		\$855,578
	Net Cash Value		\$623,775	Death Benefit at age 80		\$1,304,540

**Assumptions:**

- Tax rate assumed to be 40%
- Income and cash value based on assumed annual crediting rate of 9.03%
- Tax replacement loan rate = LIBOR+90bps (6.40%)
- Tax replacement loan and interest must be repaid prior to taking income loans
- Pre-retirement funding source, recent 457(f) distribution

Please note: All values are estimates based time, rates of interest and return. Refer to the complete insurance illustration and companion loan and distribution illustration for additional information.



# QUESTIONS



## More Information & Questions

Contact our specialists:

**Drew Erra - Senior Vice President**

**[drew.erra@IHStrategies.com](mailto:drew.erra@IHStrategies.com)**

**Tom Becker - Senior Vice President**

**[tom.becker@IHStrategies.com](mailto:tom.becker@IHStrategies.com)**

**800-327-9335**

**A recording of this Webinar can be downloaded at our web site:**

**[www.IHStrategies.com](http://www.IHStrategies.com)**



## Webinar Series Continues...

### Webinar #3 - Compensation & Benefits Update - Proposed New Regulations

Thursday April 17, 2008

1:00 PM CDT

This is **NOT** another technical review of the proposed changes to 457(f) and the new 409A regulations!

Learn how the After-Tax Protocol can eliminate the need to face the new compliance challenges.

Kirk Sherman - Sherman & Patterson, Ltd.

Sandy Enos - Senior Vice President

Moderator: David Saltzman - Senior Director of Communications

Register at: [www.IHStrategies.com](http://www.IHStrategies.com)

